

# TOOLBOX

BY

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## GIMME A BREAK

Making the most of new tax legislation in 2008.

**DOES** a tax saving of \$272 in 2008 mean anything to you? It should. That number, small though it may seem, represents a sizable investment opportunity for your clients.

The Canadian Taxpayers Federation has estimated that retroactive tax changes announced in 2007, coupled with changes taking effect in 2008, will benefit the average taxpayer by about \$272 in 2008. Reductions will be felt at both the federal and provincial levels, with only New Brunswick expecting a net increase in taxes this year.

Federal Bill C-28, officially enacted in mid-December, instituted a number of tax-reduction measures designed to increase disposable income, reduce personal and business tax, and allow investors to keep more of their gains in 2008.

### Gilding the Golden Years

With the bulk of the workforce and voting population (namely baby boomers) in pre-retirement territory, the government has wisely decided to ease the financial burden of retirement and provide some incentive for investment. Take a look at the following areas:

#### › Pension Income Splitting

This is possibly the biggest tax change for average Canadians in more than 30 years. It's estimated that the ability to split up to half of one's pension income with spouses or common-law partners will save older couples a total of \$700 million annually. This new initiative has numerous benefits. For example, a spouse continuing to earn income can minimize (and in some

cases prevent) pension income clawbacks through a transfer of income to the spouse earning little or no income.

Keep in mind that the age of your client will determine the level of income splitting entitled to him or her while under the age of 65. Eligible pension income (suitable for splitting) is limited to registered pension plans (RPPs). Clients 65 or older can also split income from RRSPs, RRIFs, and deferred profit-sharing plans.

#### › RRSP Limit Increased to Age 71

Clients turning 69 this year have an additional two years to benefit from tax-sheltered compound growth and take advantage of any unused contribution room either through opening a new RRSP or using an existing one.

Reflecting the increasing longevity of Canadians and the intent of many to remain in the workforce as long as possible, the federal government has increased the age limit for contributing to RRSPs to 71 from 69.

Money already rolled into a RRIF can be converted into an RRSP, but it must be converted back into a RRIF by the end of the year in which the person turns 71.

#### › Maximum Annual RRSP Contribution Limit Increased

This year, Canadians can shelter an additional \$1,000 in their RRSPs to a maximum of \$20,000. Stand-alone mutual funds are especially well suited to capture these relatively small amounts of potential investment capital. Funds that pay out distributions in the form of interest (such as bond funds) can preserve capital and grow tax-free within an RRSP. Usually such investments are stable, making them a good fit for retirement planning.

Here's more welcome news: RRSPs can now include any debt obligation with an invest- **continued on page 14**

**continued from page 13** ment grade rating that is part of an issuance of \$25 million or more, or any security listed on a designated stock exchange. Nevertheless, an RRSP is probably not the best place for those penny-mining stocks.

## More Ways to Invest

Raising children is an expensive proposition, but the government has provided Canadians with children ample opportunity to invest for their futures.

Some new offerings include the introduction last year of a new benefit for children under age six: the Universal Child Care Benefit (UCCB), to help with the expenses of raising pre-school age children. The UCCB is worth \$100 monthly for every child under the age of six, and is taxed in the hands of the lower-income spouse. Small but reliable amounts of capital such as these might be effectively deployed in a dollar-cost averaging strategy into a diversified portfolio of equities, which would provide the greatest growth potential over a long-term horizon. If begun at birth, by the time payments end on the child's seventh birthday, the portfolio will be well established.

And, a new Child Tax Credit stepped up relief for parents this year—and can be claimed up until a child reaches 18. The credit is calculated by multiplying the lowest personal income tax rate for the year (15.0% in 2007) by \$2,000 for each child, resulting in a tax saving of \$300 per child for the 2007 taxation year. Due to the fact the tax credit is non-refundable, any remaining credit must be transferred between eligible spouses in order not to be lost.

You will want to alert your clients to the newfound flexibility for funding Registered Education Savings Programs (RESPs). As of the last federal budget, the annual limit was eliminated and the

lifetime limit was raised to \$50,000 per beneficiary from \$42,000. In addition, the annual grant room for the Canada Education Savings Grant (CESG) was increased to \$500 per year per beneficiary from 2007 onward. If the beneficiary has carry-forward CESG room from prior years, the maximum CESG paid in one year is \$1,000. This is based on an RESP contribution of \$5,000 (every RESP dollar matched by 20%). Contributions can be made in a lump sum to maximize the opportunity for tax-free growth.

## More Needles in the Haystack

Other tax breaks worth considering as potential sources of investment capital include:

- › **Increases in the basic personal amount as well as the spousal or partner amounts to \$9,680, up from \$8,929, and retroactive to January 1, 2007.**
- › **Increase in pensionable earnings for 2008 to \$44,900, up from \$43,700.**
- › **Lowest income bracket up to \$37,178 dropped from 15.5% to 15%, retroactive to January 1, 2007.**
- › **Small business tax rate (applied on up to the first \$400,000 of active business income earned by a Canadian Controlled Private Corporation) falls from 13.1% to 11% effective January 1, 2008.**

## Good Deeds Get Rewarded

Although the hoped-for general capital gains relief failed to materialize, investors with a charitable bent can point to some positive developments.

- › **Philanthropy to offset capital gains**  
Generosity should not be taxable. It's a good time to remind your clients of the elimination last year of taxes on in-kind donations of securities, mutual funds and segregated funds to registered charities. Donating securities allows the charity to benefit and your client does not have to pay tax on capital gains,

provided the tax receipt for the donation is accompanied by form T1170.

Donations in kind can be combined with tax-efficient structures like Series T versions of mutual funds that distribute cash flow in the form of tax-deferred return of capital (ROC). Your clients meet the need for cash flow by drawing on their adjusted cost base (ACB) and can eliminate the entire tax on the gain in future by donating the securities. (Note: If the ACB reaches zero before the client donates the funds, there may be tax payable on any negative ACB.) Although December 31 was the last date to make a donation for 2007, keep this strategy in mind for the upcoming taxation year.

## Know Your Client, Know Their Investments

Unless you happen to be a tax accountant, Canadian tax law is likely peripheral to your practice. But you can still help your clients by staying current and referring tax questions to a qualified professional (ideally within your network of accounting, legal and estate professionals).

This knowledge will be invaluable when clients turn to you for advice on investment decisions. You might want to remind clients of the increasing number of tax-friendly investments available in the marketplace—such as corporate class vehicles that are being offered by many fund companies. These allow investors to meet their financial goals while deferring the capital gains tax on switches until a later date.

Above all, pay close attention to your clients' capital gain and loss positions—you can actively manage capital losses to offset gains (consult an accountant about superficial loss rules). That's where you can add value and build the kind of loyalty that will keep their assets on your books for many years to come. **AE** **TEW**